The Mergers & Acquisitions Review

Eighth Edition

Editor
Mark Zerdin

Law Business Research

The Mergers & Acquisitions Review

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THE LAW REVIEWS

THE MERGERS AND ACQUISITIONS REVIEW

THE RESTRUCTURING REVIEW

THE PRIVATE COMPETITION ENFORCEMENT REVIEW

THE DISPUTE RESOLUTION REVIEW

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EDITOR'S PREFACE

There is cause for optimism and caution in light of the past year's events.

First, we can be tentatively optimistic about Europe. The possibility of a euro breakup appears to have faded, and European equities markets performed, on the whole, exceptionally well in 2013. Indeed, the euro/dollar basis swap has moved sufficiently to open up euro capital markets to borrowers wishing to swap proceeds to dollars; the World Bank sold its first euro benchmark bond for more than four years in November 2013, and non-European companies like Sinopec and Korea Natural Gas have issued large euro bonds in recent months. If the European economy continues to grow (and analysts are expecting growth to quicken), it is hoped that the prospect of crisis will continue to fade.

Second, though 2013 was a comparatively languid year for global M&A, the buoyancy of the credit and equity markets cannot be ignored. In terms of financing, the seeming willingness of banks to allow for looser borrower constraints, to underwrite jumbo facilities in small syndicates, and to offer flexible and fast bridge-financing for high-value acquisitions, presents a financing climate that should be particularly amenable to corporate M&A. It is also notable that continued political and economic instability did not impede the completion of some standout deals in 2013, including the *Glencore/Xstrata* tie-up and Vodafone's disposal of its shareholding in Verizon Wireless. These deals show that market participants are able, for the right deal, to pull out all the stops. After a period of introspection and careful balance sheet management, corporates may be increasingly tempted to put cash to work through M&A.

There remains, however, cause for prudence. There is considerable uncertainty as to how markets will process the tapering of quantitative easing (QE) by the US Federal Reserve. The merest half-mention by Ben Bernanke, in May 2013, of a possible end to QE was enough to shake the markets, and to nearly double the 10-year US Treasury yield in a matter of months. Emerging markets are particularly sensitive to these shocks. The oncoming end of QE may already have been priced into the markets, but there is a possibility that its occurrence will cause further, severe market disruption. In addition, there are concerns around how the funding gap left by huge bank deleveraging will be

filled, and centrifugal pressures continue to trouble European legislators. Finally, there are broader concerns as to the depth of the global economic recovery as growth in the BRIC economies seems to slow. Optimism should, therefore, be tempered with caution.

I would like to thank the contributors for their support in producing the eighth edition of *The Mergers & Acquisitions Review*. I hope that the commentary in the following chapters will provide a richer understanding of the shape of the global markets, together with the challenges and opportunities facing market participants.

Mark Zerdin
Slaughter and May
London
August 2014

Chapter 36

JAPAN

Hiroki Kodate and Junya Ishii[1]

I OVERVIEW OF M&A ACTIVITY

Due to the changing Japanese and global economy, the level of M&A activity involving Japanese companies continued to be moderate throughout 2013. However, thanks to the 'Abenomics', a set of measures introduced by Japanese Prime Minister Shinzo Abe after his December 2012 re-election to the post and designed to revive the sluggish economy with 'three arrows': a massive fiscal stimulus, more aggressive monetary easing from the Bank of Japan, and structural reforms to boost Japan's competitiveness, Japanese stock has risen and the Japanese yen has weakened significantly since early 2013.

It is yet to be seen how much this will have an effect on the overall M&A activity involving Japanese companies.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

In Japan, the Companies Act and the Financial Instruments and Exchange Act (FIEA) provide the fundamental statutory framework for M&A transactions. The Companies Act provides fundamental rules concerning companies and applies to both public and closed companies, whereas the FIEA makes provision for, among other things, public offers of securities, tender offers, insider trading, and is an important source of rules regulating M&A transactions involving public companies. There are also other important laws such as the Antimonopoly Act (AMA) in which Japanese merger control rules are contained. In relation to foreign investment in Japanese companies, the Foreign Trade and Foreign Exchange Act requires the approval of, or reporting to, relevant ministries in certain circumstances.

1 Hiroki Kodate is a partner and Junya Ishii is an associate at Anderson Mōri & Tomotsune.

The listing rules promulgated by the Japanese stock exchanges provide for, *inter alia*, timely disclosure obligations and delisting requirements, which are also important for deals involving public companies.

Last, a number of recent court cases have the potential to significantly affect the M&A framework of Japan. These are described in detail in the latter part of this chapter.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i Amendments to the Companies Act

In November 2013, a bill to amend the Companies Act (the Amendment Act) was submitted to the Diet partly for the purpose of improving M&A-related regulations and is currently under discussion at the Diet. The following briefly reviews three major points regarding M&A transactions.

Third-party allocation involving a change in the controlling shareholder

Under the current Companies Act, generally speaking, where a public company intends to make a third-party allocation of its shares, a board resolution will suffice and a resolution of a shareholders' meeting is not required unless the allocation price is 'particularly favourable' to the allottee. However, even if the terms of the allocation are not particularly favourable to the allottee, if such allocation involves a change in the controlling shareholder of that company (the shareholder who owns a majority of all voting rights in respect of that company), its impact on other shareholders should be taken into account.[2]

In this regard, the Amendment Act sets out that where a public company intends to make a third-party allocation of its shares that results in the allottee holding a majority of the voting rights of all shareholders of the company, such company is required: (1) to give prior notice thereof to existing shareholders or make a public announcement of the same; and (2) except in very limited circumstances, to pass an ordinary resolution at a shareholders' meeting approving such allocation of shares if the shareholders holding one-tenth or more of the voting rights of all shareholders give notice of their opposition within a specified period.

More specifically, in the notice or public announcement in (1) above, the Amendment Act provides that the name and address of the allottee that will hold a majority of the voting rights of all shareholders and the number of voting rights that the allottee will hold as a result of the allocation in question must be included, so that enhanced disclosure can be achieved.

2 In this connection, the Tokyo Stock Exchange amended the listing rules in 2009 so that where a listed company intends to make a third party allotment of its shares which results in a dilution of 25 per cent or more or the change in a controlling shareholder, an opinion by a party independent from the company's management (such as an outside director or outside company auditor) or a shareholder resolution shall be obtained. Similarly, the Financial Services Agency of Japan also amended the disclosure guidelines in 2010 to achieve enhanced disclosure.

Although the enhanced disclosure in (1) above would not be a greater duty for listed companies that have already disclosed relevant information pursuant to the listing rules or the FIEA, there may be cases where a third-party allocation is significantly delayed by the opposition of shareholders in the case of (2) above. To avoid such a situation, it may be advisable to set a flexible schedule that takes into account possible opposition from shareholders (and the shareholders' meeting to be held), or obtain prior approval at a shareholders' meeting.

Assignment by a parent company of shares in a subsidiary

Where a parent company loses control over a subsidiary through selling its shares in that subsidiary, this may affect the parent company in a similar way to that of an assignment of business of the parent company. Under the current Companies Act, however, unlike a business assignment, there are no express provisions that state that the approval of a shareholders' meeting of the parent company is required where a parent company intends to assign its shares in its subsidiary.

The Amendment Act provides that if a company assigns all or a part of its shares in a subsidiary, the company must obtain prior approval for the assignment agreement by special resolution at a shareholders' meeting, unless: (1) the book value of the shares or units being assigned does not exceed 20 per cent (or, in cases where a lesser proportion is prescribed in the articles of incorporation, such proportion) of the value of the total assets of the parent company; or (2) on the effective date of the assignment, the parent company holds a majority of the voting rights of all shareholders of the subsidiary.

By necessitating the approval at the parent company's shareholders meeting, the sale process of the subsidiary may be delayed.

Buyout by a special controlling shareholder

The Amendment Act sets out a new provision whereby a special controlling shareholder (SCS) – a person who holds at least 90 per cent of the voting rights of all shareholders of a company – may make a demand that all other shareholders of the company sell their shares to the SCS.[3]

According to the Amendment Act, an SCS who intends to make such a demand is first required to give notice to the company about the conditions of the sale, including the amount of money to be paid to selling shareholders, and the date on which the SCS will acquire the shares. If the company gives its consent to the conditions of the sale, it must give notice to the selling shareholders no later than 20 days prior to the acquisition date, stating, *inter alia*, the details of the SCS and the conditions of the sale. By the company giving such notice, the SCS shall be deemed to have made the demand to the other shareholders for the sale of their shares, and the SCS will acquire all of the shares on the date of acquisition.

For an SCS who intends to implement a cash-out of the remaining shareholders, this new rule will speed up the process as it does not require the shareholders' meeting

3 The Amendment Act provides that these new cash out rules also apply to share options.

that is currently needed under the most general cash-out techniques under the current Companies Act. If this new rule is implemented, it would likely be used in practice.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

i Outbound transactions

Due to the increasing recognition of the importance of overseas operations among Japanese companies, last year showed that there continues to be large-scale outbound M&A transactions in which Japanese companies are acquiring high-value businesses outside Japan. A few notable examples of such transactions are as follows.

Mitsubishi UFJ Financial Group Inc/Bank of Ayudhya Public Company Limited
In July 2013, it was announced that the Bank of Tokyo-Mitsubishi UFJ Ltd (BTMU), a subsidiary of Mitsubishi UFJ Financial Group Inc, one of the largest financial groups globally, signed a share tender agreement with GE Capital International Holdings Corporation (GE Capital) regarding GE Capital's shareholding in the Bank of Ayudhya Public Company Limited (Krungsri). The voluntary tender offer launched by BTMU was completed in December 2013 with a total transaction amount of ¥536 billion and BTMU acquired approximately 72 per cent of the total issued shares of Krungsri. The transaction is part of BTMU's strategy to further develop its business in Asia and in particular to strengthen its offering of financial services in Thailand.

Development Bank of Japan Inc and LIXIL Corporation/Grohe Group S.a.r.l
In June 2013, it was announced that the Development Bank of Japan (DBJ) and LIXIL Corporation (LIXIL) entered into an agreement for the acquisition of an 87.5 per cent equity interest in Grohe Group S.a.r.l (Grohe) from private equity funds managed by TPG Capital and DLJ Merchant Banking Partners. DBJ is a financial institution wholly-owned by the Japanese government and LIXIL is the largest housing and building materials company in Japan, both are headquartered in Tokyo. Grohe is a German company which makes high-end faucets and other bathroom fixtures. The acquisition was completed in January 2014 with a total transaction amount of ¥428.4 billion, the largest ever German investment by a Japanese company to date, and Grohe and Joyou AG, Grohe's publicly listed subsidiary, became LIXIL-affiliated companies. The transaction follows LIXIL's acquisition of American Standard Brands in August 2013, Permasteelisa Group in 2011 and American Standard Asia Pacific in 2009.

ORIX Corporation/Robeco Groep NV
In February 2013, it was announced that ORIX Corporation (ORIX), an integrated financial services group based in Tokyo, would acquire approximately 90 per cent of equity in Robeco Groep NV (Robeco), a medium-sized global asset manager, from Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A (Rabobank). The acquisition was completed in July 2013 with a total transaction amount of ¥250.7 billion. The agreement embodies a strategic alliance between Rabobank and ORIX, partly reflected by Rabobank retaining a 9.99 per cent share in Robeco.

ii Inbound transactions

Applied Materials Inc/Tokyo Electron Limited

In September 2013, Applied Materials Inc (AMAT) and Tokyo Electron Limited (TEL) entered into a definitive agreement to create a new combined company via an all-stock combination which values it at approximately US$29 billion. The transaction involved AMAT (a US-based company providing equipment, services and software for the manufacture of advanced semiconductor, flat panel display and solar photovoltaic products) acquiring TEL (a supplier of semiconductor, flat panel display and photovoltaic panel production equipment) for a reported amount of US$8.7 billion thus contributing 68 per cent to the total value of inbound transactions for 2013.

The new enterprise will be incorporated in the Netherlands with a new name and will have dual headquarters in Tokyo and Santa Clara, as well as a dual listing on the Tokyo Stock Exchange and the NASDAQ. Ownership of the new company is unevenly split after the close of the transaction, with AMAT's shareholders holding approximately 68 per cent and TEL's shareholders holding approximately 32 per cent.

The business combination will create a global innovator in semiconductor and display manufacturing technology and is intended to accelerate the strategic visions of AMAT and TEL. By the end of the first full fiscal year, AMAT and TEL anticipate to reach US$250 million in annualised run-rate operating synergies, this is expected to jump to US$500 million by the third full fiscal year.

In February 2014, the companies announced that they received clearance without conditions from the Committee on Foreign Investment in the United States thus terminating their review of the transaction. However closing of the combination is still subject to customary conditions, including approval by shareholders of AMAT and TEL, as well as review by regulators in other countries.

Kohlberg Kravis Roberts & Co LP/Panasonic Healthcare Co Ltd

In September 2013, Panasonic Corporation (Panasonic) and Kohlberg Kravis Roberts & Co LP (KKR) announced the signing of a share purchase agreement and a shareholders' agreement whereby Panasonic and KKR will become joint partners in Panasonic Healthcare Co, Ltd (PHC). Panasonic is a global corporation specialising in the development and engineering of electronic technologies and KKR is a global investment firm.

Under the agreements, PHC Holdings Co., Ltd (PHCHD), which is wholly-owned by KKR, was set to purchase all outstanding shares of PHC (including its related intellectual property and assets) for an equity value of approximately US$1.67 billion. A third-party share allocation by PHCHD would then follow this transaction, leaving KKR owning 80 per cent of outstanding shares in PHCHD and Panasonic owning 20 per cent. In March 2014, the companies announced that the agreements were completed. Panasonic and KKR have agreed to cooperate in the management of PHC.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Court decision

In 2013, there were a number of notable court cases in Japan that may affect future M&A transactions. In this section, we discuss one case concerning the obligation of directors, as part of their duty of care, to transfer the fair value of the company and to disclose adequate information for the benefit of shareholders if a management buyout (MBO) occurs.

Rex Holdings Case

In April 2013, the Tokyo High Court delivered a judgment in response to a claim made by the shareholders of Rex Holdings Co, Ltd (Rex), which merged into a company known as AP8 Co, Ltd (AP8) at that time, against the directors of Rex. The shareholders of Rex sought to be compensated for damages incurred from being forced to sell off their shares in Rex at a low price through the MBO by which AP8 launched the tender offer that was followed by a squeeze-out of the remaining minority shareholders. In the judgment, the Tokyo High Court made the following decisions: (1) directors assume the duty of care to transfer the fair value of the company in the event of an MBO (however, the directors were not in breach of such duty in this case); and (2) in light of specific circumstances under the MBO in this case, the directors assumed, as a part of the duty of care, the duty to provide adequate information to the shareholders at least at the stage where Rex expressed its approval for the tender offer by AP8, and the directors were in breach of such duty in this case (however, no damage was found in this case).

With respect to the duty to transfer the fair value of the company, the Tokyo High Court stated that conducting an MBO by directors is legitimate unless there are special circumstances where doing so is considered to be a significantly unreasonable business judgment. However, given that the duty of care directors assume in relation to their company is aimed at realising common interests of the company (i.e., its shareholders) and that shareholders have common interests with respect to the MBO by which directors acquire the company at a fair buyout price appropriately reflecting the value of the company and shareholders obtain distribution of the appropriate value of the company, including the value realised by the MBO, directors who conducted an MBO at a low buyout price that does not appropriately reflect the value of the company are in breach of their duty of care. On the other hand, the Tokyo High Court stated that, as the buyout price in this case is considered appropriate according to the comparable peer company analysis and the DCF method, and thus is not considered lower than the objective value of the company, the directors were not in breach of the duty of care in this case.

With respect to the duty to disclose adequate information, the Tokyo High Court ruled that, given that the press release announcing a major downward revision to the earnings estimates of Rex caused a significant drop of the share price of Rex approximately three months before the MBO and that there was suspicion that the press release was intended to manipulate the stock price of Rex, the information regarding the said press release was necessary for the shareholders' evaluation of the appropriateness of the buyout price. Accordingly, the directors assumed the duty to provide the shareholders

with the information regarding the press release, at least at the stage where Rex expressed its approval for the tender offer by AP8, and the directors' failure to provide this information constituted a breach of their duty.

ii M&A transactions in Japan

Hitachi Ltd/Mitsubishi Heavy Industries Ltd

In November 2012, Mitsubishi Heavy Industries Ltd (MHI), one of the world's leading heavy machinery manufacturers headquartered in Tokyo, and Hitachi Ltd (Hitachi), a leading global electronics company also headquartered in Tokyo, agreed to transfer their respective operations centred on thermal power generation systems to an integrated company. In accordance with that agreement, MHI and Hitachi signed a basic integration agreement and a joint venture agreement in relation to the business integration in June 2013, and absorption-type company split agreements in July 2013. The reported value of the deal is US$3.3 billion.

The name of the new integrated company is Mitsubishi Hitachi Power Systems, Ltd (MHPS) and the equity interest of MHI and Hitachi is 65 per cent and 35 per cent respectively. It aims to be a market leader in the thermal power generation systems market, where significant expansion of global demand is anticipated. MHPS operates in the field of thermal power generations systems, including gas turbines, steam turbines, boilers, and coal gasification systems. The business of the new integrated entity also involves geothermal power systems, environmental equipment and fuel cells.

Iida Home Max Co Ltd/Hajime Construction Co Ltd

In June 2013, Iida Home Max Co Ltd, Hajime Construction Co Ltd (Hajime), Touei Housing Corp, Tact Home Co Ltd, Arnest One Corp and Id Home Co Ltd announced that the six companies will establish a holding company through a joint share transfer. In November 2013, Iida Group Holdings Co Ltd (IGH) was established as the holding company and became listed on the Tokyo Stock Exchange. The transaction targeting Hajime for US$2.1 billion was reportedly the third largest deal of the year.

IGH is principally engaged in the operation of real estate business and real estate related activities, including renovations, real estate brokerage services and mortgage loans, hot spring and golf course operations and providing internet-related consulting services. Through its subsidiaries, it is engaged in the construction and sale of detached houses and selling condominiums.

Jupiter Telecommunications Co Ltd/Japan Cablenet Limited

In November 2013, Jupiter Telecommunications Co Ltd (JCOM), Japan's largest cable TV operator, executed a share transfer agreement to acquire all the shares KDDI Corporation holds in Japan Cablenet Limited (JCN), Japan's second largest cable TV multiple system operation. In December 2013, JCOM acquired all shares of JCN for US$1.1 billion.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

LBOs have become more common in Japan in recent years. Banks operating in Japan extend loans to acquisition vehicles funded partly by equity so that these vehicles may make a tender offer over a Japanese-listed target to acquire all of the issued shares in it (the first-tier transaction) followed by a squeeze-out transaction for the remaining shareholders with the approval of shareholders of the target at a shareholders' meeting (the second-tier transaction; see above on the Amendment Act's introduction of the new cash-out rule). Extension of loans is often made in the form of syndicated loans, which involve a number of banks in the case of large-scale buyouts.

VII EMPLOYMENT LAW

In February 2014, a bill to amend the Act on the Improvement, etc. of Employment Management for Part-Time Workers for the purpose of promoting improvement of employment management for part-time workers was submitted to the Diet. The amendments included: (1) expanding the scope of the definition of 'Part-Time Workers Equivalent to Ordinary Workers' who are prohibited from being subject to discriminatory treatment as compared to ordinary workers; (2) the prohibition of unreasonable disparity between the treatment of part-time workers and the treatment of ordinary workers; and (3) imposing an obligation on employers to explain the improvement of employment management for part-time workers to newly hired part-time workers.

These regulations may become an issue that needs to be carefully considered when conducting legal due diligence for M&A transactions involving targets that hire a number of part-time workers.

VIII TAX LAW

In April 2011, Yahoo! Japan Corporation (Yahoo! Japan) filed a lawsuit with the Tokyo District Court requesting the cancellation of a disposition by the Tokyo Regional Tax Bureau (TRTB) concerning an assessment by the TRTB in which it applied Article 132-2 of the Corporate Tax Act (CTA), a catch-all anti-avoidance rule concerning corporate reorganisations (the Catch-All Rule).

In February 2009, Yahoo! Japan purchased SoftBank IDC Solutions Kabushiki Kaisha (IDC) from Yahoo! Japan's parent company for a purchase price of approximately ¥45 billion. At the time of the purchase, IDC had net operating losses (NOLs) of approximately ¥54 billion. This purchase was followed by a merger of IDC into Yahoo! Japan a month later, and Yahoo! Japan, in its 2009 tax return, deducted the NOLs that it had succeeded from IDC. Following this deduction, the TRTB conducted an audit of Yahoo! Japan and asserted that: (1) the merger lacked a business purpose; (2) the purchase price of IDC was calculated based on unrealistic data; and (3) the transaction was solely aimed at exploiting the NOLs taken over by Yahoo! Japan from IDC. The TRTB alleged that the real reason behind the merger transaction was tax avoidance and disallowed the deduction of such NOLs by Yahoo! Japan in its 2009 tax return. It also determined that Yahoo! Japan owed a tax liability of an estimated ¥26.5 billion. It

is considered to be the first time that the Catch-All Rule has been applied since it was added to the CTA in 2001 along with provisions that introduced tax-free corporate reorganisations. In March 2014, the Tokyo District Court dismissed the claim filed by Yahoo! Japan (Yahoo! Japan appealed).

Under the Catch-All Rule, the district director of a regional tax office, regardless of the contract and accounting treatment of a corporation for tax purposes, may: (1) challenge the tax benefits sought in a tax return of a corporation that is a party to a merger, corporate divisive reorganisation, in-kind incorporation, in-kind distribution, share exchange, or transfer of shares (each a 'corporate reorganisation'); and (2) assess the taxable income, losses and the amount of the tax liabilities of such corporation as the district director may see fit in certain circumstances. Specifically, the district director can make assessments where it is found that the burden of corporate tax is unjustifiably lightened by the implementation of a corporate reorganisation due to a decrease in profits or deemed dividends, increase in losses or tax credits, or for any other reason.

Under the Catch-All Rule, the phrase 'it is found that the burden of corporate tax is unjustifiably lightened' provides the district director with considerable liberty to apply this rule to various corporate reorganisations. As there are no objective standards by which to determine if a corporate tax burden has been 'unjustifiably' lightened, the language of this provision appears to allow application of this provision at the district director's sole discretion. As a general rule, however, to reduce the risk of the Catch-All Rule being applied, it is necessary to establish a non-tax business purpose for carrying out a corporate reorganisation (i.e., to choose an transaction that is commercially reasonable even without the tax benefit, rather than a solely tax-motivated transaction) to achieve the ultimately desired corporate structure. Further, the above judgment of the Tokyo District Court stated that, even if it is not considered that each of the individual actions constituting a corporate reorganisation has no business purpose, if such actions, as a whole, are clearly contrary to the intent and purpose of the tax system applicable to the corporate reorganisation, or the intent and purpose of each provision that governs individual actions, the statement that 'it is found that the burden of corporate tax is unjustifiably lightened' will apply. Given this judgment, a corporate reorganisation needs to be carried out in view of the intent of the tax law even if it is for business purposes, because the district director may make assessments with respect to actions that are contrary to the intent of the tax law.

IX COMPETITION LAW

In December 2013, the AMA was amended for the purpose of abolishing the hearing system of the Fair Trade Commission (FTC). Under this amended AMA: (1) the hearing procedure conducted by the FTC is abolished, and appeals against administrative disposition (such as cease and desist orders) imposed by the FTC are examined by the Tokyo District Court; and (2) with respect to prior procedures to the imposition of administrative disposition (such as cease and desist orders) by the FTC, the procedure for reviewing opinions presided by officials designated by the FTC is improved and the provisions concerning the inspection and copying of evidence of facts found by

the FTC are established. The amended AMA will take effect within 18 months of its promulgation in December 2013.

X OUTLOOK

Due to the Abenomics, Japanese stock remains high and the Japanese yen continues to be relatively weak. It has yet to be seen how long these trends will continue and how much they will affect the level of activity of M&A transactions involving Japanese companies.

Appendix 1

ABOUT THE AUTHORS

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